The Pakistan Credit Rating Agency Limited

HUM NETWORK LIMITED

	NEW [JUN-16]	PREVIOUS [JUN-15]
Entity		
Long Term	A+	A+
Short Term	A1	A1
Outlook	Positive	Positive

REPORT CONTENTS

JUNE 2016

Profile & Ownership

- Hum Network Limited (HNL), commenced its operations in May 2004. The shares of the company were subsequently quoted on PSX in 2005.
- HNL received a license to operate an International Satellite Television from the Pakistan Electronic Media Regulatory Authority (PEMRA) in October 2004.
- Sponsoring family holds 31% of total shares.
- A group of foreign investors/funds, though unrelated, own a significant 44% stake in HNL; Ths Kingsway Fund (25%), Stitching Bermont Limited (10%), ACACIA Partners LP (10%).

Governance

- The board comprises eight members including five from sponsoring family, one nominee of JS group, one independent and one executive director.
- From Sponsoring family directors, three are non-executive while two – ED (Sultana Siddiqui) and CEO (Duraid Qureshi) – are executives.
- The board has presence of seasoned media personalities which ensures quality oversight of the company's operations.
- Two committee namely Audit committee and human Resource & remuneration committee are formed by the board.

Management

- HNL has well-defined reporting lines and organizational structure.
- The Internal Audit function is outsourced to KPMG Taseer Hadi & Co. Chartered Accountants and reports to the Board Audit Committee.
- The CEO – Mr. Duraid Qureshi is a business graduate from LUMS.
- Majority of the senior management personnel have extensive experience working at senior positions with the state-owned Pakistan Television Corporation (PTV).

Systems & Controls

- HNL has multiple agreements with various satellite providers for transmission operation services.
- The company has two in house studios and an off-site studio along with eight editing suites.
- HNL has installed latest digital archiving system comprising LTO-6 tapes.
- HNL is planning to switch its transmission on HD technology in the near future.
- The company is integrating ERP system with modules of oracle financials to improve its internal control framework.

Business Risk

- Amidst declining advertisement revenue HNL increased its net revenue by ~7% mainly with the help of film distribution revenue (9MFY16: PKR 235mln; 9MFY15: Nil).
- HUM TV one of HNL's premiere channel witnessed a decline in its share in number of minutes advertised (CY15: 6%; CY14: 8%).
- Increased cost of outsourced programs, led to decline in business margins (Gross Margin: 9MFY16: 35%; 9MFY15: 50%; Operating Margin: 9MFY16: 14%; 9MFY15: 25%) consequently, HNL booked lower profit in 9MFY16: PKR 332mln (9MFY15: PKR 554mln).
- Going forward, the management plans to strengthen its existing revenue streams. Meanwhile, to manage the cost of outsourced programs HNL intends to acquire Momina Duraid Productions – a leading production house. Furthermore, HNL expects further growth in the cinema industry also plans to increase its film distribution revenue under its brand - HUM FILMS.

Financial Risk

- HNL's working capital requirement mainly arises due to its high receivables.
- HNL's net cash cycle days increased YoY owing to higher inventory and receivable days (end-Mar16: 106 days; end-Mar15: 84days).
- During 9MFY16, HNL's free cash flow from operations (FCFO) – declined mainly due to lower profitability. Thus, HNL's coverages dropped yet remain strong (FCFO/Gross Interest: end-Mar16: 6.8x; end-Jun15: 29.6x; end-Mar15: 26.2x).
- The company continues to enjoy strong financial profile given low leveraging.

RATING RATIONALE

The ratings reflect HNL's strong market position in the domestic media industry. HNL enjoys sound financial profile supported by good coverages and low leveraging - though increased a bit lately. On performance side, stiff competetion kept the business margin under check; thus lower profitability. To further strengthen and diversify its revenue stream, HNL is expanding its viewer ship in different geographies. Moreover, HNL is establishing income stream through (i) film distribution under the brand of "HUM Films" and (ii) ancillary domains including publications and holding events. The management expects improvement in performance as a result of these initiatives. However, these impacted the company's working capital cycle which witnessed further extension in the recent period. The same was funded through a combination of cashflow from operations and borrowings. The ratings recognize HNL's experienced management team having sound understanding of the media industry.

KEY RATING DRIVERS

The ratings are dependent on the company's ability to diversify its revenues while perpetuating margins at an adequate level. Meanwhile, any stress on financial profile either by decline in business margins, in turn, weakened operational cash flows or by further material increase in working capital cycle, would affect the ratings. At the same time, upholding governance standards would remain important.

Hum Network Limited *PKR mln*

BALANCE SHEET	31-Mar-16	30-Jun-15	30-Jun-14	30-Jun-13
	9M	Annual	Annual	Annual
Non-Current Assets	**876**	**785**	**496**	**464**
Investments (Others)	**210**	**135**	**98**	**19**
Current Assets	**1,950**	**1,869**	**1,362**	**1,290**
Inventory (Finished Goods)	489	526	311	291
Trade Receivables	1,241	1,037	776	682
Other Current Assets	217	293	168	161
Cash & Bank Balances	4	14	107	156
Total Assets	**3,035**	**2,789**	**1,955**	**1,772**
Debt	**550**	**358**	**4**	**3**
Short-term	495	300	-	-
Long-term (Inlc. Current Maturity of long-term debt)	**55**	**59**	**4**	**3**
Trade Payables	633	355	286	172
Due to Associates	-	-	-	-
Provision for Taxation	-	100	4	-
Other Liabilities	14	305	265	141
Shareholder's Equity	**1,838**	**1,671**	**1,396**	**1,456**
Total Liabilities & Equity	**3,035**	**2,789**	**1,955**	**1,772**
INCOME STATEMENT				
Turnover	**2,836**	**3,721**	**2,870**	**2,291**
Gross Profit	1,003	1,845	1,382	996
Operating Profit	395	968	740	518
Other Income	62	6	18	12
Financial Charges	(28)	(24)	(8)	(7)
Taxation	(98)	(285)	(215)	(177)
Net Income	**332**	**747**	**592**	**388**
CASH FLOW STATEMENT				
Free Cashflow from Operations (FCFO)	188	696	648	480
Net Cash changes in Working Capital	162	684	658	479
Net Cash from Operating Activities	113	167	730	325
Net Cash from InvestingActivities	(151)	(178)	(131)	(69)
Net Cash from Financing Activities	(364)	(681)	(648)	(50)
Net Cash generated during the period	(401)	(692)	(49)	206
Closing Balance of Cash & Equivalents	(491)	(286)	107	156
RATIO ANALYSIS				
Performance				
Turnover Growth	54.5%	29.6%	25.3%	31.5%
Gross Margin	35.4%	49.6%	48.1%	43.5%
EBITDA Margin	0.0%	28.2%	27.8%	24.5%
Net Margin	0.0%	28.2%	27.8%	24.5%
ROE	18.3%	52.6%	44.5%	27.5%
Coverages				
Debt Service Coverage				
1. (FCFO/Gross Interest+CMLTD) (X)	4.7	16.5	67.6	51.4
2. (FCFO/Gross Interest+CMLTD+Uncovered STB) (X)	4.7	16.5	67.6	51.4
Interest Coverage				
1. (FCFO/Gross Interest) (X)	6.8	29.6	81.4	64.0
2. (EBITDA/Gross Interest) (X)	18.4	47.9	107.3	82.0
Liquidity and Cashflows				
Current ratio (X)	1.7	1.8	3.6	5.7
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	106.4	84.7	91.1	99.6
Capital Structure (Total Debt/Total Debt+Equity)	23.0%	17.6%	0.3%	0.2%

STANDARD RATING SCALES & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

LONG TERM RATINGS

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances or economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk**. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business, and economic environment.
CCC CC C	**Very high credit risk**. "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

SHORT TERM RATINGS

A1+: The highest capacity for timely repayment.

A1:. A strong capacity for timely repayment.

A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.

A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, a suspended rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, or e) the entity/issuer defaults.

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Rated Entity

Name of Rated Entity Hum Network Limited
Sector Media
Type of Relationship Solicited

Purpose of the Rating — Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Rating Watch
30-Jun-15	A+	A1	Positive	-
30-Jun-14	A+	A1	Stable	-
16-May-13	A+	A1	Stable	-
12-Jul-12	A+	A1	Stable	-
16-Jul-11	A	A1	Stable	-

Related Criteria and Research — Electronic Media - Viewpoint | Jun-16

Methodology: — Corporate Rating Methodology

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Rating Team Statement

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